

November 18, 2005

The Honorable Frank H. Murkowski, Governor  
Members of the Alaska State Legislature  
Alaska Retirement Management Board  
Employers and Plan Members of the System

We are pleased to present the Comprehensive Annual Financial Report (CAFR) of the Public Employees' Retirement System (PERS) (System) for the fiscal year ended June 30, 2005.

This report is intended to provide comprehensive information on the financial operations of the System for the year. Responsibility for the accuracy, completeness, and fairness of the information presented rests with the management of the System. To the best of our knowledge and belief, the enclosed information is accurate in all material respects and is reported in a manner designed to present fairly the financial position and results of operations of the System for the year ended June 30, 2005. All disclosures necessary to enable the reader to gain an understanding of the System's activities have been included.

For financial reporting purposes, the System utilizes Governmental Accounting Standards Board (GASB) Statement No. 25, *Financial Reporting for Defined Benefit Pension Plans and Note Disclosures for Defined Contribution Plans*; GASB Statement No. 34, *Basic Financial Statements – and Management's Discussion and Analysis – for State and Local Governments*; GASB Statement No. 37, *Basic Financial Statements – and Management's Discussion and Analysis – for State and Local Governments: Omnibus*; GASB Statement No. 38, *Certain Financial Statement Note Disclosures*; and GASB Statement No. 40, *Deposits and Investment Risk Disclosures*. Assets of the System are presented at fair value. The actuarial value of assets and the actuarial accrued liability are presented in the required supplementary information following the notes to the financial statements.

The CAFR is divided into five sections:

- **Introductory Section**, which contains this letter of transmittal, the administrative organization of the System, and a list of the members serving on the Public Employees' Retirement Board and the Alaska Retirement Management Board;
- **Financial Section**, which contains the Independent Auditors' Report, management's discussion and analysis (MD&A), basic financial statements, required supplementary information, and additional information;
- **Investment Section**, which contains a message from the Chair of the Alaska State Pension Investment Board (ASPIB), a list of members serving on the ASPIB, a report on investment activity, investment results, and various investment schedules;
- **Actuarial Section**, which contains the Actuarial Certification letter and the results of the most current (June 30, 2003) annual actuarial valuation; and
- **Statistical Section**, which includes graphs and tables of significant data.

The PERS was established in 1961 to provide pension and postemployment healthcare benefits for eligible state and local government employees. Normal service, survivor, and disability benefits are available to all members who attain the age and service requirements of the System.

	PERS		
	2005	2004	2003
Net Assets (millions)	\$8,590.7	8,177.3	7,391.5
Participating Employers	160	161	160

### Reporting Entity

The System is considered a component unit of the State of Alaska for financial reporting purposes. Because of the closeness of the System's relationship to the State, it is included in the State of Alaska CAFR as a blended component unit.

The Commissioner of the Department of Administration, appointed by the Governor, is responsible for administering the System. In order to meet the statutory requirements of administering the System, the Commissioner appoints the Director of the Division of Retirement and Benefits. The Director is responsible for the daily operations of the System.

Prior to July 1, 2005, the Public Employees' Retirement Board (Board) prescribed policies and regulations, heard appeals, and approved employers' contribution rates prepared by the System's independent actuary.

Prior to October 1, 2005, the ASPIB had statutory oversight of the System's investments and the authority to invest the System's monies.

The Alaska Retirement Management Board (ARMB) was constituted effective October 1, 2005, and replaces the Public Employees' Retirement Board and the ASPIB. The ARMB is responsible for:

- adopting investment policies and developing investment objectives;
- providing a range of investment options and establishing the rules by which participants can direct their investments among those options, when applicable;
- establishing crediting rates for member's individual contribution accounts, when applicable;
- assisting in prescribing policies for the proper operation of the System;
- coordinating with the System Administrator to have actuarial valuations performed;
- reviewing actuarial assumptions and conducting experience analyses;
- contracting for an independent audit of actuarial valuations and external performance calculations;
- providing a report to the legislature fifteen days after the first day of the legislative session on the short-term and long-term recommendations for addressing the unfunded liability of the System; and
- reporting to the governor, legislature and individual employers participating in the PERS on the financial condition of the system.

The Department of Revenue, Treasury Division (Treasury), is responsible for carrying out investment policies established by the ASPIB prior to October 1, 2005, and the ARMB beginning October 1, 2005. Actual investing continues to be performed by external investment firms and Treasury staff listed in the Investment Section of this report.

### **Major Initiatives**

The System continues to make progress on completing several on-going projects. Most of these efforts focused on improvements in technology, improving methods for members to obtain information about the System and their benefits, and continued compliance with accounting requirements of the Governmental Accounting Standards Board (GASB) and the Financial Accounting Standards Board (FASB) as applicable.

The Public Employees' Retirement Board looked at ways to reduce costs to the employers and address the unfunded status of the System while also balancing the need to provide adequate benefits in order to effectively recruit and retain new members. Senate Bill 141 was passed during the 2005 legislative session creating Tier IV in the PERS. This new tier is a defined contribution plan and becomes effective for members entering the system on or after July 1, 2006.

### **Independent Audit**

The System's annual audit was conducted by the independent accounting firm of KPMG LLP. The auditors' report on the basic financial statements is included in the Financial Section of this report.

### **Actuarial Valuation**

The actuarial firm, Mercer Human Resource Consulting, Inc., completed the actuarial review and valuation as of June 30, 2003, and served as technical advisor to the System. Actuarial certifications and supporting statistics are included in the Actuarial and Statistical Sections of this report.

### **Professional Services**

Professional consultants are retained to perform professional services that are essential to the effective and efficient operation of the System. A list of consultants is provided in the Introductory Section with the exception of investment professional consultants, who are listed in the Investment Section of this report.

### **Certificate of Achievement**

The Government Finance Officers Association of the United States and Canada (GFOA) awarded a Certificate of Achievement for Excellence in Financial Reporting to the Alaska Public Employees' Retirement System for its comprehensive annual financial report for the fiscal year ended June 30, 2004. In order to be awarded a Certificate of Achievement, a government must publish an easily readable and efficiently organized comprehensive annual financial report. This report must satisfy both generally accepted accounting principles and applicable legal requirements.

A Certificate of Achievement is valid for a period of one year. We are confident our current comprehensive annual financial report continues to meet the Certificate of Achievement Program's requirements. Therefore, we are submitting it to the GFOA for consideration.

## Future Employer Contribution Rates

The System's consulting actuary presented the results of the June 30, 2003, actuarial valuation report to the Administrator and the Board. The assumptions and benefits are explained in the Actuarial Section of this report.

Based on the most recent valuation report (June 30, 2003), the System has a funding ratio (assets of the System divided by the total liabilities for pension and postemployment healthcare) of 72.8%. The unfunded portion of the System's liabilities totals approximately \$2.9 billion. The unfunded liability is amortized over a 25-year period, as established by the Board. In order to bridge the gap between assets and liabilities of the System, the employer contribution rate is projected to increase over the same 25-year period from the fiscal year 2004 rate of nearly 12 percent to approximately 34 percent in fiscal year 2028, if the System's actual experience agrees with the assumptions underlying the valuation. The current asset allocation that the ASPIB set for the System's investments is expected to provide a five year median return of 7.84 percent.

There are three primary reasons that have contributed to the System's current funding ratio: (1) loss of investment income; (2) rising health care costs; and (3) change in assumptions. These three factors coupled together have negatively impacted the funding ratio for PERS and resulted in increasing employer contribution rates.

For additional information on how a defined benefit system like PERS operates, the Division has developed a "white paper" that describes how the System is funded and where the System costs are. This "white paper" is titled "Employee Benefits and Retirement System Funding" and is located at: [www.state.ak.us/drdb/news/retirement-system-funding.pdf](http://www.state.ak.us/drdb/news/retirement-system-funding.pdf).

Currently, the Alaska PERS is among the few retirement systems that pre-fund and account for medical costs. The PERS system is fortunate in that the creators and administrators of the System had foresight to fund the healthcare costs in advance. Most other major governmental retirement systems only account for their current annual liability for healthcare costs. Once GASB Statement No. 43, *Financial Reporting for Postemployment Benefit Plans Other than Pension Plans*, is implemented, all systems will account for their future healthcare costs making comparisons between systems more meaningful. Implementation will occur with the largest plans no later than the financial reporting period beginning after December 15, 2005. The smallest plans will implement no later than the financial reporting period beginning after December 15, 2007.

## Acknowledgments

The preparation of this report is made possible by the dedicated service of the staff of the System. It is intended to provide complete and reliable information as a basis for making management decisions, as a means of determining compliance with legal provisions, and as a means of determining responsible stewardship of the System's monies.

The report is available on the web at [www.state.ak.us/drdb/pers/perscafr.shtml](http://www.state.ak.us/drdb/pers/perscafr.shtml) and mailed to those who submit a formal request. This report forms the link between the System and the membership. The cooperation of the membership contributes significantly to the success of the System. We hope the employers and plan members find this report informative.

November 18, 2005

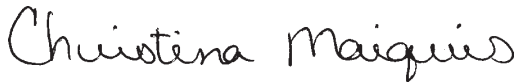
We would like to take this opportunity to express our gratitude to the Public Employees' Retirement Board, the Alaska State Pension Investment Board, the staff, the advisors, and to the many people who have worked so diligently to assure the successful operation of the System.



Scott J. Nordstrand  
Commissioner



Kevin Brooks  
Deputy Commissioner



Christina Maiquis, CPA  
Defined Benefits Accounting Supervisor

Respectfully submitted,



Melanie Millhorn  
Director



Charlene Morrision, CPA  
Chief Financial Officer

# Certificate of Achievement for Excellence in Financial Reporting

Presented to

Alaska Public Employees'  
Retirement System,  
Alaska

For its Comprehensive Annual  
Financial Report  
for the Fiscal Year Ended  
June 30, 2004

A Certificate of Achievement for Excellence in Financial Reporting is presented by the Government Finance Officers Association of the United States and Canada to government units and public employee retirement systems whose comprehensive annual financial reports (CAFRs) achieve the highest standards in government accounting and financial reporting.

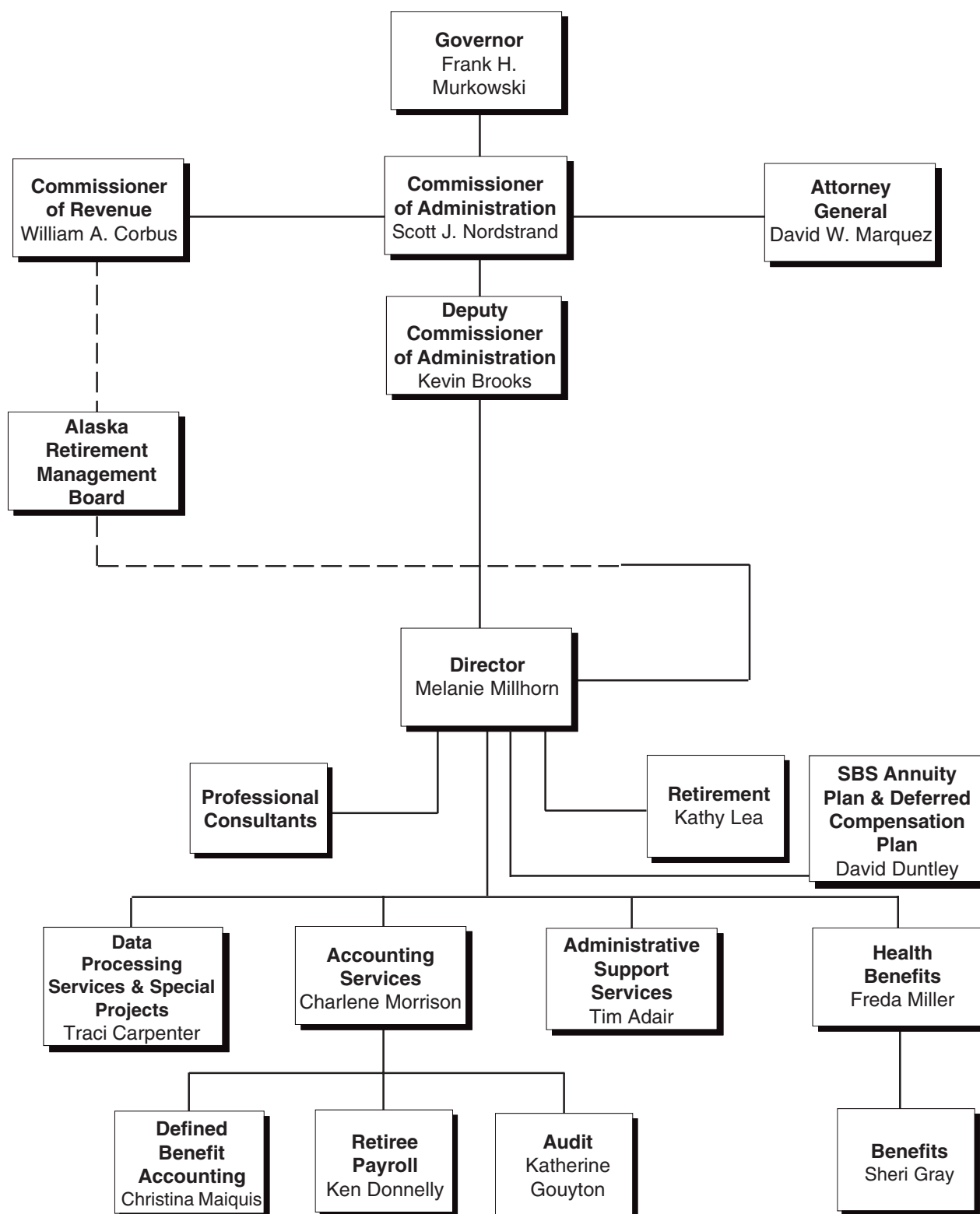


*Nancy L. Ziehl*

President

*Jeffrey R. Emer*

Executive Director

**ORGANIZATION CHART**  
**(as of November 15, 2005)**

## Section Responsibilities

The **Retirement Section** is responsible for providing comprehensive retirement counseling to the participating members and employers in the plan. This section appoints members to retirement benefits and maintains benefit payment information.

The **Benefits Section** is responsible for the administration of group health, disability, and life insurance. This section provides benefits counseling and plan change information to the membership.

The **Defined Benefit Accounting Section** is responsible for maintaining the employee and employer records and accounts in each of the defined benefit plans administered by the Division, producing financial statements and reports, and assuring compliance with the Internal Revenue Service requirements for defined benefit plans.

The **Defined Contribution Accounting Section** is responsible for accounting, plan operations, and financial activities related to the defined contribution plan systems administered by the Division.

The **Data Processing Services Section** supports the information systems the System uses. Responsibilities include planning, development, data base design, programming, and operational support of the data processing systems, including the Local Area Network.

The **Administrative Support Services Section** is responsible for budget preparation, fiscal management of appropriations, procurement of professional services, supplies, and equipment. The section manages the systems' record center containing the member's physical records and performs other administrative functions such as legislative tracking and personnel management.

The **Retiree Payroll Section** is responsible for issuing monthly and on-demand retirement benefit payments to eligible retirees or their beneficiaries. The section maintains accurate records for reporting benefit recipient tax statements and reporting and paying withheld income taxes, garnishments, and IRS levies.

### PROFESSIONAL CONSULTANTS

**Consulting Actuary**

Mercer Human Resource Consulting  
*Seattle, Washington*

**Independent Auditors**

KPMG LLP  
*Anchorage, Alaska*

**Benefits Consultant**

Deloitte & Touche, LLP  
*Minneapolis, Minnesota*

**Third Party Health Claim Administrator**

Aetna Life Insurance Company  
*Walnut Creek, California*

**Legal Counsel**

Virginia Ragle  
Toby Steinberger  
Assistant Attorney Generals  
*Juneau, Alaska*

**Legal Counsel - Retirement Boards**

Wohlforth, Johnson, Brecht, Cartledge & Brooking  
*Anchorage, Alaska*

**Consulting Physicians**

Kim Smith, M.D.  
William Cole, M.D.  
*Juneau, Alaska*

A list of external money managers and consultants for the System can be found on pages 60-61, and the Schedule of Investment Management Fees on pages 68-69.



## PUBLIC EMPLOYEES' RETIREMENT BOARD

(as of June 30, 2005)



### **George Sullivan, Chair**

George Sullivan grew up in Alaska. After graduation from Valdez High School, he joined the Army during WWII and served in the Aleutians. George represented the Anchorage area in the legislature in the mid 60's and was mayor of Anchorage from 1967 to 1982. He has always been active in the community and continues to give leadership to a number of organizations in Alaska, including the Anchorage Senior Center, Boys and Girls Club, Enstar Gas Board, Pioneers of Alaska, and the Veterans of Foreign Wars. George lives in Anchorage with his wife, Margaret. They divide their retirement days between a very appreciative community and the families of their 9 children, which include 15 grandchildren and 1 great-grandchild.



### **Alyce Hanley, Vice Chair**

Alyce Hanley has lived in Anchorage since 1971. She graduated from high school in Pawtucket, Rhode Island, and completed her nurse's training at the New England Deaconess Hospital School of Nursing in Boston, Massachusetts. She was elected to the Anchorage School Board in 1981 and to the Alaska House of Representatives in 1984. After serving three terms, she chose not to run for re-election. In 1993, Mrs. Hanley was appointed to serve as a Commissioner with the Alaska Public Utilities Commission. She retired from that position in April 1999.

Alyce enjoys family activities with her five sons, their wives and seven grandchildren, all of whom live in the Anchorage area.



### **Bronk Jorgensen**

Bronk Jorgensen was born in Jackson Hole, Wyoming. He became an Alaskan resident in 1978, before he was one year old. Bronk attended Tok School, the University of Alaska Fairbanks, and attended the University of Pittsburgh, Semester at Sea program, graduating with a degree in Business Administration.

Bronk lives in Tok and is the owner/manager of All Alaska Gifts and Crafts and Jorgensen Realty. He is also a member of the Tok and State of Alaska Chambers of Commerce and was the 2002 recipient of the Chuck West New Pioneer Award from the Alaska Travel Industry Association.

Bronk enjoys Alaska's hunting, fishing, and outdoor activities.



### **Frank Narusch**

Frank Narusch has been an Alaskan resident since 1952. Raised in the coal mining camp of Suntrana on the Healy River, he boarded away to attend high school at Monroe High School in Fairbanks and Copper Valley School in Glennallen. While attending Seattle University, he worked summers commercial fishing in Cordova, coal mining in Suntrana, and surveying and inspecting projects around Fairbanks and Valdez for the Department of Highways (now DOT&PF). After receiving a degree in civil engineering in 1966, he began his professional career with the Department of Highways. During his 31 years of State employment, he held positions as Construction Project Manager, Regional Materials Engineer, Contract Claims Engineer, and Professional Services Chief. While with the State, he was active with the Alaska Public Employees Association.

He enjoys weekly breakfast get-togethers with retired friends as well as summer travel, camping, and exploring back roads around the state.



### **James "Pat" Wellington**

Pat Wellington was born in Ketchikan, Alaska, and graduated from Douglas High School. He served two years in the U.S. Army and started his law enforcement career with the Seward Police Department in late 1955. He served as Deputy U.S. Marshal, Alaska State Troopers; Chief of Police of Juneau; Deputy Commissioner and Commissioner of the Department of Public Safety; and retired in 1977 as Director of the Alaska State Troopers. Mr. Wellington is also a trustee of the Alaska State Pension Investment Board.

## ALASKA RETIREMENT MANAGEMENT BOARD

The Alaska Retirement Management Board (ARMB) replaced the Public Employees' Retirement Board and the Alaska State Pension Investment Board effective October 1, 2005. The ARMB is made up of nine members appointed by the Governor. Initial ARMB members and their related term expiration dates are as follows:

Commissioner of Administration – Scott J. Nordstrand

Commissioner of Revenue – William A. Corbus

Two public members who are not members or beneficiaries of either the PERS or TRS:

Gail Schubert, Chair (March 1, 2007)

Martin R. Pihl (March 1, 2008)

One political subdivision finance officer – Lawrence A. Semmens (March 1, 2007)

Two members of the PERS:

Sam Trivette, Vice Chair (March 1, 2006)

Michael R. Williams (March 1, 2008)

Two members of the TRS:

Gayle W. Harbo, Secretary (March 1, 2006)

John R. Roses (March 1, 2008)

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